

December 16, 2003

The Honorable Mayor and
City Commissioners
City of Mount Clemens
One Crocker Boulevard
Mount Clemens, MI 48043

Dear Mayor and Commissioners:

We have completed our audit of the financial statements of the City of Mount Clemens for the year ended June 30, 2003. In addition to our audit report, we offer the following comments and recommendations for your consideration:

NEW FINANCIAL STATEMENT FORMAT (GASB 34)

As you are aware, Governmental Accounting Standards Board (GASB) Statement No. 34 was implemented for the City's 2003 fiscal year. GASB 34 has dramatically changed the look and feel of the financial statements. While the financial statements retain an element of familiarity with the continued reporting of fund based information, there are several additions and changes that provide information never before presented in the City's annual financial report. A brief summary of the changes are as follows:

- *Management Discussion and Analysis (MD&A)*: The MD&A provides a high-level overview of the City's financial position and results of operations, with a focus on the government-wide financial statements.
- *Government-Wide Financial Statements*: These additional statements adjust the normal fund-based statements into a combined, full-accrual format (similar to for-profit commercial enterprises). This allows a financial statement reader to see the City from a longer term, economic perspective (i.e. are today's taxpayers paying for today's services?). These statements show capital and infrastructure assets, as well as long term debt as part of the City's overall financial picture.
- *Focus on Major Funds*: The fund based financial statements now focus on the City's most significant funds (major funds). For 2003, the City's major governmental fund is the General Fund; all of the City's enterprise funds are considered to be major funds.
- *Budget Comparison*: A financial statement reader will now be able to view not only the actual revenues and expenditures for the City's major governmental funds as compared to the current budget, but also as compared to the original budget.

Capital assets, including infrastructure, play a significant part of the new financial statements. The accumulation of this information required significant investment of the City's resources, both financial and non-financial, primarily in the form of a physical appraisal performed by an outside party with the assistance of City personnel. The detailed asset information obtained will most likely also be useful for insurance and asset control purposes. For this reason, it is extremely important that the information be transferred into the City's records and kept current. We would be pleased to assist the City in developing a plan for updating and developing capital asset records.

OVERVIEW OF THE CITY'S FINANCIAL CONDITION

During the year ended June 30, 2003, General Fund expenditures exceeded revenues by approximately \$944,000 taking into account transfers to other funds. Fund balance at June 30, 2003, totaled approximately \$3,045,000. Of this amount, \$2,640,000 is designated specific purposes, including capital improvements, currently unfunded post-employment benefit obligations, and other purposes, and the remaining \$405,000 is undesignated.

The City continues to be faced with budgetary challenges. Many challenges, including further reductions in State revenue sharing payments, are a direct result of the difficult economic period that has been experienced in the State of Michigan. Other challenges, such as the limited ability to experience growth in property tax revenue, future capital equipment and infrastructure needs and currently unfunded post-employment benefit obligations, are a characteristic of the City and its physical framework. We encourage the City Commission and administration to continue to closely monitor the budget to ensure that fund balance reserves are adequate.

We also recommend that the five-year financial forecasting model be updated to allow the City to better predict the effects of revenue changes and what impact those changes have on the City's ability to provide services. It is important that the City maintain an adequate level of working capital and fund balance to adjust to financial changes without affecting the level of services provided to citizens or the City's ability to fund future obligations.

STATE REVENUE SHARING

Reduced sales tax collections and significant budget shortfalls at the State of Michigan continue to negatively impact the City as a result of reduced State shared revenue payments. State shared revenue payments, which totaled approximately 20 percent of the 2003 General Fund Budget, decreased from the payments received in 2002. Further reductions will be experienced in the 2004 fiscal year as described below. Revenue sharing payments are affected by reduced sales tax collections; these reductions are further compounded by cuts made by the State to balance its budget.

The original budget for the State's fiscal year ended September 30, 2004, included a three percent reduction in revenue sharing payments from the estimated payments for the State's 2003 fiscal year. The State's most recent revenue estimating conference indicated that sales tax collections are significantly below the estimates used to generate the 2004 budget; as a result, the State has made further cuts to statutory revenue sharing payments in order to balance its budget. As a result, total revenue sharing payments for 2004 are expected to be approximately 9 percent less than what were received in 2003.

We recommend and it is our understanding that the City will continue to evaluate the impact of the revenue sharing reductions on the 2003-2004 budget. Updated information can be obtained from the Department of Treasury's web site at <http://treas-secure.state.mi.us/apps/findrevshareinfo.asp> or by calling the Office of Revenue and Tax Analysis at (517) 373-2697. We will continue to update the City as developments occur.

REVENUE BOND COVENANTS

The City is subject to bond covenants for the revenue bond issues in the Water Supply and Sewage Disposal Funds. Specifically, the City is required to maintain and restrict adequate cash reserves for operation and maintenance of the systems, debt service payments, and additional bond reserves. At June 30, 2003, the City's cash balances in the Water Supply and Sewage Disposal Funds fell approximately \$987,000 short of the reserve requirements. We recommend that the City continue to evaluate Water and Sewer user rates in order to ensure that all debt service requirements and the bond covenants are met in the future.

ELECTRONIC FUND TRANSFERS (ACH TRANSACTIONS)

Recently, Public Act 738 was passed, which allows local units of government to make and accept electronic funds transfers (ACH payments), if the City adopts a formal policy. While local units of government may have already been using the ACH system for payroll tax remittances and for the direct deposit of payroll, this new law requires a policy to be adopted.

We recommend that the City Commission consider adopting a policy on ACH arrangements that includes all of the following:

- Designation of an individual as the party responsible for payment approval, accounting, reporting and compliance with the ACH policy;
- A statement that this individual is required to submit documentation as follows:
 - describe the goods or services purchased,
 - the cost,
 - date of payment, and
 - the department benefiting from the purchase;
- A system of internal controls to monitor the use of ACH transactions; and
- The approval of ACH invoices before payment.

We would be happy to assist the City in developing an appropriate policy.

FUNDING OF POST-EMPLOYMENT BENEFIT OBLIGATIONS

As you are aware, the City provides post-employment benefits to retirees that are funded currently from the General Fund. For the year ended June 30, 2003, the cost of these benefits amounted approximately \$1,318,000, representing an increase of approximately 24 percent over the 2 amount. The City has experienced post-employment health care cost increases of 15 to 30 p

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over the past several years and this annual cost is expected to continue grow as the average age of the City's workforce and the number of former employees eligible for post-employment benefits increases.

We recommend that the City consider establishing a Retiree Health Care Fund to begin to set aside resources to fund these obligations. A fund that is established in accordance with The Public Employee Health Act of 1999 (P.A. 149 of 1999) would allow the City to invest assets set aside for post-employment benefit obligations in the same investment vehicles as pension funds (e.g. stocks, bonds, etc.). These investments provide a better means of achieving rates of return necessary to fund these long-term liabilities.

We also recommend that the City also consider evaluating and funding post-employment benefit obligations on an actuarial basis, similar to pension obligations. Current accounting pronouncements do not require accounting for post-employment on an actuarial basis, however, a proposed standard by the Governmental Accounting Standards Board includes provisions for measuring post-employment benefit liabilities and expenses on an actuarial basis. Furthermore, actuarial funding generally provides the best mechanism for funding obligations over long time periods and multiple budget cycles.

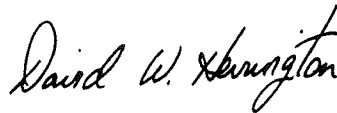
NEW HOMESTEAD AUDIT PROGRAM

Public Act. 105 of 2003 provides new authority for local units of government and the Michigan Department of Treasury to share homestead information to determine if a resident is inappropriately claiming an homestead exemption on property. As you recall, following the passage of Proposal A in 1994, individuals in Michigan are allowed only one homestead for property tax purposes. A residence which is not an individual's homestead pays property tax at the non-homestead rate. The Michigan Department of Treasury will provide additional guidance related to this new law.

We would like to thank the Mayor and City Commission for the opportunity to serve as auditors for the City. We would also like to express our appreciation for the courtesy and cooperation extended to us by the administration during the audit. If you would like to discuss any of these matters, or would like assistance in their implementation, please contact us.

Very truly yours,

PLANTE & MORAN, PLLC



David W. Herrington



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